

SLA

THE SURPLUS LINE
ASSOCIATION OF CALIFORNIA

Information for Legislators and Regulators

This informational brochure will explain who and what we are, who we represent, and how important and necessary our industry is to California's insurance consumers and the state's economy.

www.slacal.com

Introduction



Thank you for your interest in the Surplus Line Association of California (SLA) and in the surplus line insurance industry.

If you are not already familiar with our organization or our industry, you are not alone. Because the everyday insurance needs of most consumers are covered by insurers who are admitted to sell insurance in the State of California, our segment of the industry is largely unknown and often overlooked. However, without surplus line (or nonadmitted) insurance, many California businesses would not be able to obtain coverage, and neither those businesses, nor the consumers they serve, would be protected. Additionally, without the protection of insurance, many companies or industries that contribute significant amounts of jobs and taxes to this state would not choose to conduct business at all, if the risks outweighed the benefits. **More than 100,000 California businesses, which pay \$17 billion annually in state and federal taxes, employ 1.75 million workers and pay them more than \$50 billion a year, rely on surplus line insurance.**

One of the most enduring myths about surplus lines is that this type of business is unregulated, but the nonadmitted market in California is well and diligently regulated. In fact, 21 sections of the California Insurance Code (1760 through 1780) deal specifically with surplus lines, and all brokers who place nonadmitted policies in

the State of California are required to be licensed and in compliance with all state laws and regulations governing the industry. The SLA, appointed in 1994 as the statutory surplus lines advisory organization to the California Department of Insurance (CDI), helps brokers remain in compliance; we examine every nonadmitted filing placed in California (approximately 600,000 per year) to ensure that our members comply with all the legal requirements necessary to place policies lawfully in the state.

Our mission is to ensure that a responsive and lawful surplus lines insurance market is maintained in California. Our measure of success in this respect is that the consumer is protected, the needs of the regulators are well-served, and unlawful activities are curtailed. Through a professional and committed organization, utilizing state of the art technology, we respond to the needs of the California consumer, our membership, and appropriate public agencies. We provide education, processing, evaluation, and dissemination of surplus line data and information to help ensure the financial integrity and stability of the nonadmitted market.

We look forward to working together with you to help ensure a fair, healthy and competitive surplus lines marketplace for California insurance consumers.

Sincerely,

A handwritten signature in black ink that reads "Benjamin J. McKay". The signature is written in a cursive, flowing style.

Benjamin J. McKay, J.D., M.P.A.
Executive Director
Surplus Line Association of California

Senior Staff



Benjamin J. McKay, JD, MPA
Executive Director

Ben McKay joined the SLA in 2012 after a career in both the private and public sector. Previously, Ben spent eight years with the Property Casualty Insurers Association of America (PCI) as Senior Vice President for Federal Government Relations. In that role, Ben was named one of Washington, D.C.'s top lobbyists five times by The Hill, one of the city's leading political newspapers.

Prior to his time at PCI, Ben served as Chief of Staff to a member of the United States Congress in Washington, D.C., and worked on financial services and international relations issues. Other career highlights include eight years as staff to members of the Florida legislature, where he worked on insurance, economic development, banking, criminal justice and other important issues. He then served a tour as a regulator at the Florida Department of State, where he served as Deputy Secretary for International and Legislative Affairs and later as the youngest Chief of Staff in the history of the 750-employee department. Ben received his Juris Doctor from Catholic University, his Master in Public Administration from Harvard University, and his Bachelor of Science from Florida State University.



Pamela Boyes, SPHR, SHRM-SCP
Vice President, Human Resources

As Vice President, Human Resources, Pamela oversees the day to day human resources, facilities (including reception and mailroom), and office safety functions. She is responsible for administering the SLA's compensation and benefits plans, ensuring the Association's compliance with federal, state, and local employment laws, recruitment, payroll, performance management, employee relations, coordinating internal training, and maintaining

the employee handbook.



Clifton Brown
Vice President, Communications and Government Relations

As Vice President, Communications and Government Relations, Clifton is responsible for ensuring SLA members receive timely, high-quality communications about SLA and news affecting surplus lines brokers doing business in California. He serves as editor-in-chief of the SLA's newsletter, SLA Connection, publishes news alerts to members and manages the SLA's social media presence.

He also spearheads the SLA's communications efforts with legislators and regulators at the state and federal level.



Joy Erven, MBA
COO and Director

As Chief Operating Officer and Director, Joy is responsible for overseeing accounting, purchasing, banking and financial investments. Joy prepares and presents the annual budget and quarterly financial statements, and she interfaces with auditors for the annual financial audit. She also leads the SLA's stamping office function which oversees broker compliance with state laws and regulations.



Susan Bryant, MBA
Senior Vice President, Financial Analysis

As Senior Vice President, Financial Analysis, Susan coordinates SLA participation in the security review program for the insurance commissioner's List of Approved Surplus Line Insurers (LASLI). Susan represents the SLA at periodic meetings with the California Department of Insurance (CDI), and provides input on SLA compliance with the CDI Plan of Operation.



Michael Caturegli
Vice President, Technology

As Vice President, Technology, Michael and his department are responsible for all computing technology, office equipment, and telecommunications at the Surplus Line Association. He is responsible for ensuring that all internal employees and SLA members have the automated tools they need to access information and be in compliance. The Technology Department supports its end-users and continually keeps up with industry trends relating to technology

and automation in the marketplace.



Pat McAuley, CPCU, AIM, AIS, ASLI, AINS

Senior Vice President, Education and Compliance

As Senior Vice President of the Education and Compliance Department, Pat provides guidance, education and support to the association's membership and affiliates in their understanding of California's surplus line laws. Her department develops and provides Continuing Education (CE) courses throughout the state, and she works closely with various

departments within the California Department of Insurance (CDI).

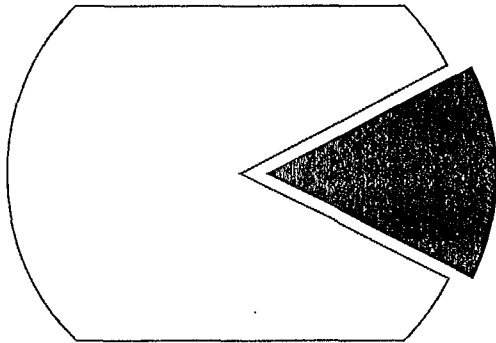


THE SURPLUS LINE
ASSOCIATION OF

CALIFORNIA

UNDERSTANDING CALIFORNIA'S SURPLUS LINE MARKET

Californians produce many important items that cannot always be insured in the standard insurance market. Surplus line insurance enables Californians to cover the risk involved in producing many of these goods, which they would not be able to produce without adequate insurance coverage.



Approximately 18 percent of all commercial insurance premiums collected in California are in surplus lines.*

What types of products do surplus lines policies insure?

29% 
FINANCIAL SERVICES

- Banks and Non-Depository Credit Institutions
- Securities Brokers and Investment Offices
- Real Estate
- Insurers
- Insurance Agents and Brokers

10% 
MANUFACTURING

- MINING
- AGRICULTURE
- Crops and Livestock
 - Processed Food
 - Forestry
 - Fishing, Hunting and Trapping
 - Textile Products
 - Apparel and Other Finished Products
 - Wood Products, Furniture and Fixtures
 - Paper, Printing and Publishing Chemicals
 - Petroleum Refining
 - Rubber and Plastics
 - Leather, Stone, Clay, Glass and Concrete
 - Industrial Machinery and Computer Equipment
 - Electronic Equipment and Components
 - Transportation Equipment
 - Medical and Optical Goods
 - Watches and Clocks
 - Extraction of Metals, Coal, Oil, Gas and Non-Metallic Minerals

37% 
GOODS AND SERVICES

- Hotels, Rooming Houses, Camps, Lodges
- Auto Repair
- Motion Pictures
- Amusement and Recreational Services
- Museums and Art Galleries
- Zoos
- Furniture and Merchandise Stores
- Restaurants
- Automotive Dealers and Gas Stations
- Durable and Non-Durable Wholesale Goods

23% 
INFRASTRUCTURE

- Railroads
- Motor Freight
- Postal Services
- Water, Pipelines
- Transportation Services
- Electric, Gas and Sanitary Services
- Construction, General Contractors and Operative Builders

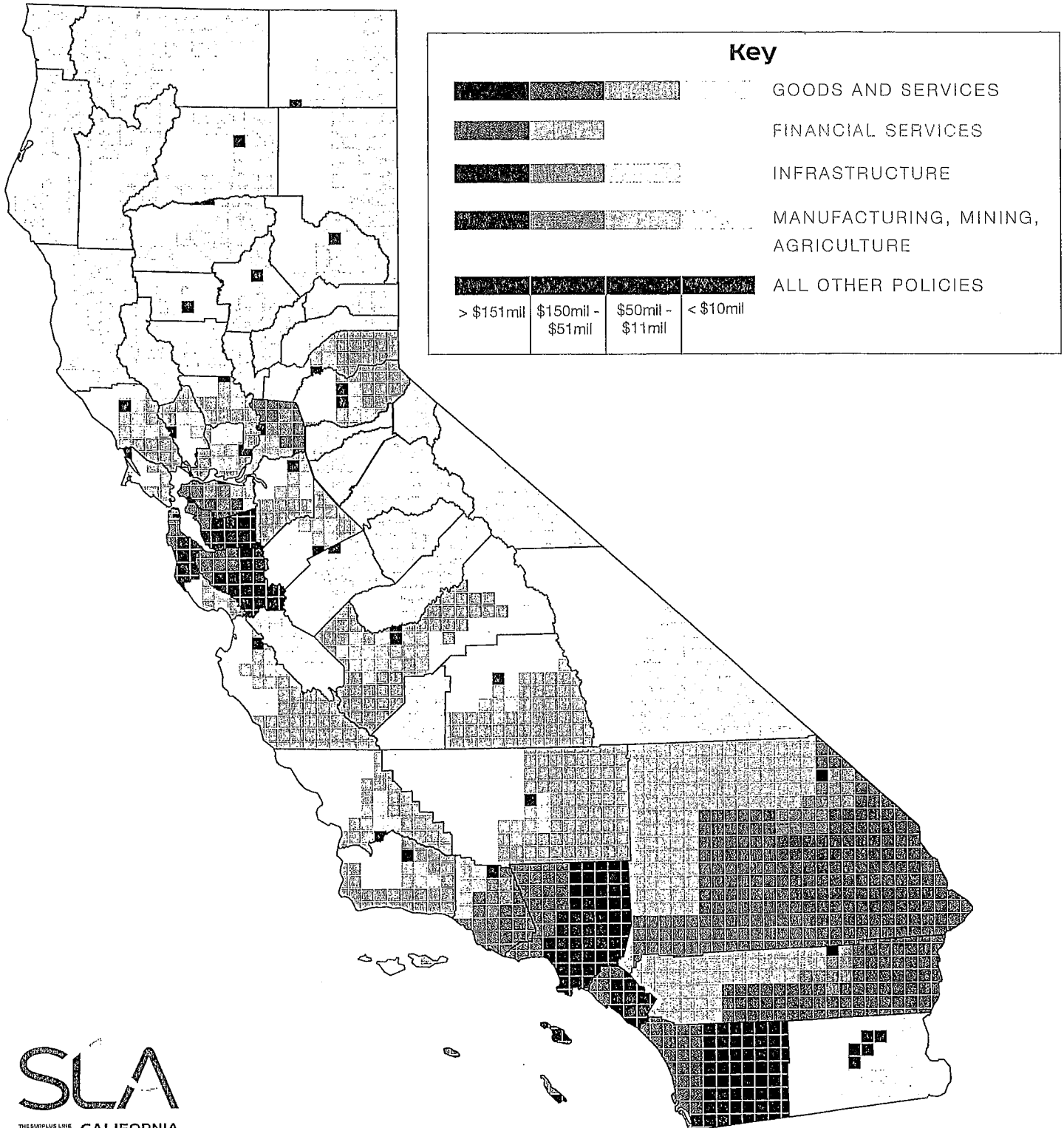
2% 
ALL OTHER POLICIES

- Public Administration
- Non-Classifiable Establishments
- Other Miscellaneous Policies

* Findings based on all policies filed with the SLA of California

THE GEOGRAPHY OF CALIFORNIA'S SURPLUS LINE MARKET

This map shows how all regions of the state benefit from the availability of surplus line insurance and gives an indication as to the impact that these insured products have in various parts of the state.*



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* Findings based on all policies filed with the SLA of California

Surplus Line Market Basics

The Surplus Line Market is a Well-Regulated and Well-Functioning Market

The surplus line market is often misunderstood. The surplus line market is not unregulated, as some believe. Surplus line insurance carriers are regulated in their domiciliary jurisdictions and must be eligible under federal and California law before business can be placed with them (exported to them). Additionally, the surplus line broker in California is licensed and regulated directly by the California Department of Insurance (CDI). Surplus Line brokers are also subject to periodic audits by the California Department of Insurance. In summation, the surplus line market is a well-functioning, well-regulated market that serves as an appropriate place for consumers to obtain coverage when the admitted market is unable to meet their insurance needs.

State and Federal Regulations

There are 21 sections of the California Insurance Code devoted to regulating surplus lines. Sections 1760 through 1780 provide the surplus line broker licensing requirements, policy placement conditions with a surplus line insurer, and the prerequisites of a surplus line insurer writing business in California.

Surplus Line Broker Licensing Requirements

To transact business as a surplus line broker, a resident broker must hold a property and casualty (P&C) license, which requires passing the fire and casualty examination for broker-agents, before applying for a surplus line license. In addition to holding a P&C license in their resident state, a non-resident broker must also hold a surplus line license in his/her resident state before applying for a surplus line license. The broker must complete an application, complete a Surplus Line and/or Special Line Certification form stating the applicant has read the sections of the California Insurance Code pertaining to surplus lines, and file a surety bond of \$50,000 to the people of the State of California.

To maintain the surplus line license, the resident broker must complete a renewal application and pay a fee to renew his/her license every two years. To maintain the P&C license, the resident broker is required to complete continuing education each license term. The non-resident broker must complete the continuing education required by his/her state of residence.

For an applicant applying for a business entity surplus line license, brokers transacting under the organizational license must be named under the license and a surety bond of \$50,000 must be filed to the people of the State of California.

Conditions of Placement with a Surplus Line Insurer

Before a risk is placed in the surplus line market, the surplus line broker must ensure that insurance is not generally available from admitted insurers qualified to write that type of insurance. Except for narrow exemptions for commercial insureds, specialty lines, and coverages listed on the "export list" maintained by the CDI, brokers must complete an affidavit (Diligent Search Report or SL2 form) documenting the diligent search effort to place the risk in the admitted market. Insurance buyers must sign a disclosure statement (D1 form) acknowledging that the risk is being placed with a nonadmitted insurer and that guaranty fund protection is unavailable to the buyer. If the SL2 form shows that three admitted insurers that actually write the particular type of insurance decline the risk or fewer than three admitted insurers write the type of insurance, it is prima facie evidence that a diligent search was made.

The broker must not place insurance with a surplus line insurer solely for obtaining a premium less than the lowest premium offered by an admitted carrier. A premium tax is levied on all surplus line transactions to the insured with payment remitted to the CDI by the broker. The broker must submit the policy and required documents to the stamping office for review to verify that the placement was handled correctly by the broker.

Brokers are audited by the Premium Tax Audit Bureau of the CDI to ensure compliance with tax filings.

Eligibility Requirements for a Surplus Line Insurer

Surplus line insurers on the List of Approved Surplus Line Insurers (LASLI) must demonstrate their financial stability, reputation and integrity; maintain a minimum of \$45 million in capital and surplus at all times; have three years' seasoning (or qualify for an exception); have a valid license to transact insurance in their domicile; file financial information with the CDI; and adhere to specific capitalization, investment and solvency standards established under the California Insurance Code.

On July 21, 2011, the federal Nonadmitted and Reinsurance Reform Act (NRRRA) went into effect, establishing federal guidelines for surplus line insurer eligibility in all states. The SLA worked with California regulators to adapt California law to the new federal standards, which led to the creation of Assembly Bill 315. AB315 established the requirements for surplus line insurers not on the LASLI to write policies in California:

- **Foreign companies** (U.S. companies domiciled outside California) must maintain a minimum capital and surplus of \$45 million and be authorized to transact in their state of domicile.
- **Alien companies** (domiciled outside the United States) must be included on the NAIC's Quarterly List of Alien Insurers.

Frequently Asked Questions

Q. What is surplus line insurance?

A. The surplus line market (also known as excess lines or nonadmitted market) is comprised of insurers who provide coverage that is unavailable to businesses in the admitted market, generally for distressed, unique or high-capacity risks that standard insurers will not cover. In general, surplus line insurance covers risks that standard insurance, such as what you might purchase for your vehicle, will not cover.

Q. What is the difference between admitted and surplus line (nonadmitted) insurers?

A. Admitted insurance companies are licensed to sell insurance in a state and are subject to that state's rate and form regulations, while nonadmitted insurance companies are not; they may be licensed in another state or country. Instead, surplus line brokers, who place business with these nonadmitted carriers on behalf of consumers, are licensed by the state.

Q. Why are surplus line insurers needed?

A. For insurance consumers who cannot secure insurance from admitted companies, the surplus line market provides additional capacity and innovative underwriting practices that admitted carriers cannot offer. Without the surplus line market, businesses might be forced to self-insure their exposures, or go without coverage. Surplus line policies protect both these businesses and the customers they serve.

Q. What types of risks do surplus line policies cover?

A. There are many types of risks that the surplus line insurance market covers. It would be impossible to provide a comprehensive list here, but some examples include large commercial construction projects, film and entertainment productions, oil field contractors, special agricultural and logging risks, some flood and earthquake risks, tattoo parlors, amusement parks and carnivals, just to name a few.

Q. Why have I never heard of surplus line insurance before?

A. The average insurance consumer's personal insurance policies, such as auto or homeowners' insurance, are generally written by admitted carriers. The overwhelming majority of surplus line coverage is written to insure commercial risks.

Q. What does the surplus line marketplace mean to California's economy?

A. Surplus line insurers provide insurance that would otherwise be unavailable for distressed, unique or high-capacity risks. Without the surplus line marketplace, those businesses would not be able to operate in the capacity they do, or perhaps even at all, due to the liability concerns involved, which would mean fewer jobs and fewer services for Californians. Additionally, surplus line policies generate approximately \$6 billion in annual premiums in California, and that premium volume alone provides a considerable amount of tax revenue to the state.

Q. What is the purpose of the Surplus Line Association of California (SLA)?

A. The SLA monitors surplus line brokers who do business in California and helps them comply with all state surplus line laws and regulations when they write business. All surplus line policies written in the state must be filed with SLA so that it may review all filings for compliance and ensure that premium taxes are collected. The California insurance commissioner in 1994 designated the SLA as the surplus line advisory organization for the California Department of Insurance (CDI). While the SLA has no specific regulatory power, it assists the CDI in ensuring broker compliance with all applicable laws and regulations.

Q. Is the SLA a private, public, or nonprofit organization?

A. The SLA is a 501(c)(6) not-for-profit organization governed by a plan of operation approved by CDI and the SLA Board of Directors.

Q. How is the SLA funded?

A. The SLA levies a small fee, called a "stamping fee," on every surplus line policy filed. While the fee may vary from year to year, depending on the anticipated needs of the organization, it is generally a fraction of 1 percent of the total premium charged on each policy. (At the time of the publication of this document, the fee was 0.2 percent, or \$1 in stamping fees for every \$500 charged in premiums.) These stamping fees are paid by the consumers who take out surplus line policies. **The SLA receives no public funding for its operations from the state of California or its taxpayers.**



Mission Statement

Our mission is to ensure that a responsive and lawful surplus line insurance market is maintained in California. Our measures of success in this respect are that the consumer is protected, the needs of the regulators are well-served, and unlawful activities are curtailed. Through a professional and committed organization, utilizing state-of-

the-art technology and a challenging work environment, we respond to the needs of the California consumer, our membership, and appropriate public agencies. We provide education, processing, evaluation, and dissemination of surplus line data and information to help ensure the financial integrity and stability of the surplus line market.